

SUMMARY OF OPTIONS FOR EMPLOYER & UNION PLAN SPONSORS

Introduction: Employment-based retiree health insurance has been an important source of drug coverage for many Medicare beneficiaries. For well over a decade, the availability and generosity of employment-based retiree health coverage has been eroding, particularly for future retirees. As prescription drug costs have risen, employers have shifted more of those costs to their retirees, and many employers have ceased offering retiree health coverage altogether.

The Medicare prescription drug benefit and the new retiree drug subsidy represent additional funding sources to help employers and unions continue to provide high quality prescription drug coverage for their retirees. Other plan sponsor options are also made possible by the statute. These new sources of support will have important positive benefits for the quality and security of drug coverage for retirees. The implementation of Medicare prescription drug coverage, including the plan sponsor options summarized below, are expected to result in combined aggregate payments by plan sponsors and Medicare for drug coverage on behalf of retirees that will be greater – and frequently significantly greater – than plan sponsors alone otherwise would have made without the enactment of the MMA.

Overview of Retiree Drug Subsidy: The retiree drug subsidy is designed to encourage employers and unions to continue providing high quality prescription drug coverage. It has highly flexible rules that permit employers and unions to continue providing drug coverage to their Medicare-eligible retirees at a lower cost while retaining their current plan designs that are at least equivalent to the value of the defined standard Part D drug benefit. The retiree drug subsidy will pay 28 percent of retiree's drug costs (as defined by the regulation) between \$250 and \$5000 in 2006. The payments are tax-free, which increases their value to plan sponsors that are subject to taxation. To qualify for the subsidy, the plan sponsor must show that its coverage is as generous as, or more generous than, defined standard coverage under the new Medicare prescription drug benefit. The final regulation includes a two-part test for plan sponsors to determine whether this standard, referred to as "actuarial equivalence," has been met. The subsidy only applies to retirees eligible for but not enrolled in a Part D plan.

Overview of Additional Plan Sponsor Options: In addition to the retiree drug subsidy discussed above, another option available to plan sponsors is to encourage their retirees to enroll in a plan that offers coverage under the Medicare prescription drug benefit (a Part D plan) while opting to provide them with extra help. There are several ways that employer and union plan sponsors can supplement the standard Medicare drug benefit:

- They can set up their own separate supplemental plans and coordinate benefits with the coverage offered by Part D plans their retirees enroll in to provide extra help with cost sharing in much the same way they currently supplement the standard Medicare Part A and B benefits.
- They can pay for enhanced coverage through a Part D plan to subsidize more of their retirees' cost-sharing and provide additional benefits. CMS plans to use its waiver authority to allow sponsors to make special arrangements with Part D plans for, or offer

their own Part D plans to, their retirees. These waivers would allow employers to provide more flexible benefits and to limit enrollment to their retirees.

- Regardless of whether they choose to provide additional coverage that supplements the standard Medicare prescription drug coverage, plan sponsors can also provide extra help by assisting their retirees in paying for some or all of their Part D beneficiary premiums.

Comparing Options. Employers and unions are likely to pick the option that is most advantageous to both the employer/union and their retirees. Factors they are likely to consider include trends in retiree health costs, changes in accounting requirements relating to post-retirement health benefits, changing demographics, the economy, and labor relations. Over time, some employers and unions may choose to transition from providing drug coverage that qualifies for the retiree subsidy in order to take advantage of other opportunities for continuing to provide high quality retiree drug coverage, including providing their own enhanced Part D plan (through waivers), purchasing enhanced part D coverage, or providing supplemental drug coverage that wraps around Medicare Part D.

All of the options available to employers and unions under Part D reduce the costs associated with providing coverage. We estimate plan sponsors that choose to participate in the retiree drug subsidy program will receive \$668 on average in annual per capita retiree subsidy payments. For plan sponsors subject to taxation, we estimate that the \$668 tax-free retiree drug subsidy would be equivalent to about \$891 of taxable income for employers with a marginal tax rate of 25 percent and about \$1,028 of taxable income for employers with a marginal tax rate of 35 percent. Meanwhile, we estimate that plan sponsors that choose to offer comprehensive drug coverage by wrapping around or enhancing Part D will achieve cost savings of at least \$900 on average due to the Federal government subsidizing a significant portion of the cost of standard Part D coverage.

Future Guidance and Outreach. We plan to issue additional guidance on a range of issues for which commenters indicated additional direction would be helpful. For example, we plan to provide guidance on the actuarial equivalence standard, the subsidy application process, and the streamlined approach CMS plans to use in implementing the employer waivers. We respect plan sponsors' need to have the guidance as soon as possible due to the complexity and timing of the process.

We will continue to conduct outreach to various groups to educate the stakeholders on the requirements for applying for the retiree drug subsidy and taking advantage of the other options available to employers and unions for continuing to provide assistance with their Medicare-eligible retirees' drug costs.

For More Information: You can visit the CMS Website at <http://www.cms.hhs.gov>.